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No. 190. OCTOBER TERM, 1908.

Office Supreme Court, U.
FILED.
MAR 8 1909
JAMES H. McKENNE
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IN THE

Supreme Court of the United States

Joseph Wild & Company, Appellants,

vs.

The Provident Life & Trust Company, Trustee of the Estate of George Watkinson & Company, Bankrupts, Appellee.

APPEAL FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT.

APPELLEE'S BRIEF.

ARTHUR G. DICKSON,
For Appellee.

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Of Counsel.

Allen, Lane & Scott, Prs., Phila.

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I. STATEMENT OF FACTS.

Briefly stated the facts of the present case are as follows:—

The bankrupts were insolvent during the entire time covered by the transactions between them and the creditor, but the latter had no knowledge of their insolvency. On February 14th, 1901, a sale was made to the bankrupts and payment therefor was received on June 29th. Between June 5th and 29th, sales were made amounting to six hundred thirty-four dollars and seventy-eight cents

($634.78). Between July 19th and October 8th, there were other sales amounting to two thousand five hundred sixty-five dollars and ninety-two cents ($2565.92). The first of these amounts, namely six hundred thirty-four dollars and seventy-eight cents ($634.78) was paid to the creditor, after the date of all of the sales, on October 10th. His claim was filed for the amount of two thousand five hundred and sixty-five dollars and ninety-two cents ($2565.92), and the position of the trustee in bankruptcy is that it should not be allowed (Bankruptcy Act of 1898, Sec. 57 G) unless the payment of six hundred thirty-four dollars and seventy-eight cents ($634.78) is surrendered, in which case the claim would be increased by that amount. The creditor's claim was allowed by the Referee, but the District Judge of the Eastern District of Pennsylvania adopted the trustee's view and the Circuit Court of Appeals for the Third Circuit has affirmed the judgment.

ARGUMENT.

The proceedings in this estate began in 1901. In 1903 the Bankrupt Act was amended so as to eliminate all questions of so-called "innocent preferences" and the question now before this court is no longer of any importance except to the creditor who seeks to retain the payment received on account of the bankrupts' indebtedness and to the trustee, representing the other creditors who have not been so fortunate.

When this court decided the case of Pirie *vs.* Chicago Title & Trust Co., 182 U. S., 438 (1901), it was enforcing the Act as it then read (Sec. 60 A.):—

> "A person shall be deemed to have given a preference if, being insolvent, he has procured or suffered a judgment to be entered against himself in favor of any person, or made a transfer of any of his property, and the effect of the enforcement of such judgment or trans-

fer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class."

This language, applicable to the present case, was held by this court to apply to creditors who have innocently received preferences.

In order to avoid the effect of the rule thus laid down, an effort was early made to give to an innocently preferred creditor the advantage given by Section 60c of the Act to one who had received a guilty and voidable preference, namely, the right to set off subsequent credits against the amount which would otherwise have to be surrendered. In several cases it was accordingly held that an innocently preferred creditor should not be placed in a worse position than one who had received a guilty preference, as, by the new credits which he had given to his debtor, the creditor had, in effect, returned payments which were otherwise preferential. Some of these cases are:—

McKay *vs.* Lee, 105 Fed., 923, S. C., 5 A. B. R., 267 (1901), Circuit Court of Appeals for the Seventh Circuit, Grosscup, J.;

In re Ryan, 105 Fed., 760, S. C., 5 A. B. R., 396 (1900), District Court, Northern District of Illinois, Kohlsaat, District Judge;

In re Southern Overall Mfg. Co., 111 Fed., 518, S. C., 6 A. B. R., 633 (1901), District Court, Northern District of Georgia, Newman, District Judge, affirmed under the name of Kahn *vs.* Export & Com. Co., 115 Fed., 290, S. C., 8 A. B. R., 157 (1902);

In re E. O. Thompson's Sons, 6 A. B. R., 663 (1901), District Court, Eastern District of Pennsylvania, Hunter, Referee, affirmed in 7 A. B. R., 214 (1902), McPherson, District Judge, affirmed by Circuit Court of Appeals for the Third Circuit under the name of Gans *vs.* Ellison, 114 Fed., 734, S. C., 8 A. B. R., 153 (1902);

Peterson *vs.* Nash Brothers, 112 Fed., 311, S. C., 7 A. B. R., 181 (1901), Circuit Court of Appeals for the Eighth Circuit, Adams, District Judge;

In re Beswick, 7 A. B. R., 395 (1900), District Court, Northern District of Ohio, Remington, Referee.

As soon as the theory that an innocently preferred creditor was entitled to the privilege of setting off against the payments received by him, the subsequent credits which he had given to his debtor, had begun to make headway, there appeared a further theory which was but the logical outcome of it, namely, that, where credits succeeded payments and the credits during the period of insolvency exceeded the payments made during the same period, it was not necessary for the creditor to make any surrender before proving his claim.

This view appears to have been first stated in the case of *In re* Jourdan, generally referred to as that of Dickson *vs.* Wyman, which is reported in 111 Fed. Rep., 726, S. C., 7 A. B. R., 186 (1901). The opinion of the Circuit Court of Appeals for the First Circuit in that case was delivered by Putnam, Circuit Judge. That case was one where numerous payments and sales had been made, the sales exceeding the payments, and the last payment, on August 8th, was succeeded by a sale on August 10th. It will be noticed, therefore, that that case was one in which, if at all, the principle could be applied.

The same view was adopted in the following cases:—

Morey Mercantile Co. *vs.* Schiffer, 114 Fed. 447, S. C., 7 A. B. R., 670 (1902), Circuit Court of Appeals, Eighth Circuit, Sanborn, Circuit Judge;

In re Kimball vs. Rosenham Co., 114 Fed. Rep., 85, S. C., 7 A. B. R., 718 (1902), Circuit Court of Appeals, Eighth Circuit, Sanborn, J.

In re Sagor & Bro., 121 Fed., 658, 9 A. B. R. 361 (1903), Circuit Court of Appeals, Second Circuit, Lacombe, Circuit Judge.

When, finally, the question reached this court in the case of Jaquith *vs.* Alden, 189 U. S., 78 (1903), the views of the Circuit Courts of Appeals for the First, Second, Third and Eighth Circuits were adopted and it was ruled that "Payments on a running account, *where new sales succeed payments,* and the net result is to increase the value of the estate, do not constitute preferential transfers under Section 60a."

On one subsequent occasion the question was raised in this court in the case of Yaple *vs.* Dahl-Millakan Grocery Co., 193 U. S., 526 (1904). This case involved a question certified by the Circuit Court of Appeals for the Sixth Circuit, which stated that sales and payments had been made during the four months prior to the bankruptcy, the sales exceeding the payments. The question did not cover the whole period of insolvency and it was not stated whether the payments or sales were last in point of time, the increase during the period named alone being called to the attention of this court. It appears, however, from the paper book of the appellant in that case, that the last of the transactions between the parties was a sale from the creditor to the bankrupt and not a payment from the bankrupt to the creditor. The case appears to have had no effect upon the law, this court stating that the question was answered by the case of Jaquith *vs.* Alden, *supra.*

The history which has thus briefly been sketched shows that the return of the innocently received preference by subsequent credits was an essential part of the theory which permitted the retention of the payments that had been received by the creditor during insolvency and within four months of bankruptcy. It is true that, in the Jaquith *vs.* Alden case, the sale which was the last of the transactions was not large enough to be by itself a return of the payment just previously received, but it was at least a partial return of that payment. Furthermore, the payments and sales were very closely inter-related, so that this court was able to regard all of the transactions as one continuing course of dealing, where payments had had the effect of inducing new sales. When the sales and payments in the Jaquith *vs.*

Alden case are examined, it is seen that there were, first, two sales, then two payments; next three sales, then a payment, and, lastly, a sale. The payments, therefore, kept the account alive and helped to increase the estate by inducing the extension of additional credits.

In the present case, the first sale was paid for and then there followed a number of sales. If the transactions had stopped there, this case would not be before this court. There was, however, a subsequent payment of a part of the account. This payment did not induce any subsequent credits; it was not so intermingled with other payments and sales as to entitle the creditor to ask that it be taken as part of a continuing transaction by which the estate was benefited. Its only effect was to reduce the estate, to take a part of the assets which then belonged to all of the creditors of the bankrupts and to give it to one of them. No reasoning, however plausible, can rob this payment of that effect and it was, therefore, under the Bankruptcy Act of 1898, a preference.

The decision of the Circuit Court of Appeals in this case was in accord with its own previous opinion in the case of Gans *vs.* Ellison, 114 Fed., 734, S. C., 8 A. B. R., 153 (1902), in which it was said:—

> "If, then, a creditor innocently preferred has given return credits afterwards he has surrendered his preference to the extent of such return credits. To effectuate justice, both sides of the account are to be considered, in the case of a creditor who innocently has received preferences, and afterwards in good faith has given the debtor further credit, without security, for property which has become a part of the debtor's estate."

The attention of this court is likewise respectfully called to the language of Sanborn, Circuit Judge, in delivering the opinion of the Circuit Court of Appeals for the Eighth Circuit, in the case of Kimball *vs.* Rosenham Co., 114 Fed., 85, S. C., 7 A. B. R., 718 (1902), and to

that of Lacombe, Circuit Judge of the Circuit Court of Appeals for the Second Circuit, in the case of Colton Export and Import Company, 121 Fed., 63, S. C., 10 A. B. R., 14 (1903).

In the former case, Judge Sanborn said:—

> "It may be said that before the $850 was paid, the claim of the Rosenham Company was $2728.13, that after its payment it was only $1878.13, and that the moment the payment was made the creditor had secured thereby a preference. *This would undoubtedly have been true if the account and the transaction had closed there.*"

And in the latter case, Judge Lacombe said:—

> "Appellant calls attention to the circumstance that all the loans were made to the bankrupt while it was insolvent, but there is no distinction recognized in the Act between claims which accrued before and after insolvency. Section 60c (Act July 1st, 1898, Chap. 541, 30 Stat., 562, U. S. Com. St., 1901, page 3446), does not apply, because the creditor has not given the debtor further credit after receiving a preferential payment. The facts are not similar to those in the line of cases which are cited *in extenso in re*. Sagor, *supra*. Payments made by the debtor have not been succeeded by new extensions of credit, and there is no room for the argument that it should be assumed that the payment induced the credit, or that the transaction is the same as if the debtor paid part cash for a new lot of goods and obtained new credit only for the balance."

Although Circuit Judge Gray, in delivering the opinion of the Circuit Court of Appeals for the Third Circuit in this case, admitted "that the authorities are not harmonious and do not satisfactorily dispose of the precise question here presented," it is submitted that, when the cases are carefully examined, there is no real difference

of opinion between the judges of different circuits. In no case, with the exception of *In re.* Topliff (114 Fed., 323 S. C., 8 A. B. R., 141 (1902), a decision by the District Court of Massachusetts) has there been a decision enabling a creditor, whose last transaction with the bankrupt during insolvency and within four months of bankruptcy, has been the receipt of a payment, to retain such payment. In every other case in which the creditor has been permitted to retain payments received during insolvency and within the four months' period, those payments have been succeeded by new credits extended to the bankrupt. As has already been stated, the only effect of the payment in the present case was to reduce the estate and it was, therefore, a preference.

The judgment of the District Court, affirmed by the Circuit Court of Appeals, should be allowed to stand.

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For Appellee.

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